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ARIZONA, COLORADO, MONTANA,
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DISTRICT OF COLUMBIA

August 28, 2008

Docket Control
Arizona Corporation Commission
1200 West Washington
Phoenix, Arizona 85007

Arizona Corporation Commission
DOCKETED

AUG 29 2008

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Re: Tucson Electric Power Company
Docket Nos. E-01933A-07-0402 and
E-01933A-05-0650

To Whom It May Concern:

Enclosed for filing in the above-referenced dockets are the original and fifteen (15) copies of a Post-Hearing Brief on behalf of Mesquite Power, L.L.C., Southwestern Power Group II, L.L.C., Bowie Power Station, L.L.C. and Semptra Energy Solutions LLC.

Please advise me in the event you have any questions. Thank you in advance for your assistance.

Sincerely,

Angela R. Trujillo
Secretary
Lawrence V. Robertson, Jr.

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BEFORE THE ARIZONA CORPORATION COMMISSION

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COMMISSIONERS

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MIKE GLEASON, Chairman
WILLIAM A. MUNDELL
JEFF HATCH-MILLER
KRISTIN K. MAYES
GARY PIERCE

AZ CORP COMMISSION
DOCKET CONTROL

IN THE MATTER OF THE APPLICATION OF) DOCKET NO. E-01933A-07-0402
TUCSON ELECTRIC POWER COMPANY)
FOR THE ESTABLISHMENT OF JUST AND)
REASONABLE RATES AND CHARGES)
DESIGNED TO REALIZE A REASONABLE)
RATE OF RETURN ON THE FAIR VALUE OF)
ITS OPERATIONS THROUGHOUT THE)
STATE OF ARIZONA.)

IN THE MATTER OF THE FILING BY) DOCKET NO. E-01933A-05-0650
TUCSON ELECTRIC POWER COMPANY TO)
AMEND DECISION NO. 62103.)
POST-HEARING BRIEF OF
INTERVENOR MESQUITE ET AL.

I.

INTRODUCTION

Mesquite Power, L.L.C., Southwestern Power Group II, L.L.C., Bowie Power Station, L.L.C. and Sempra Energy Solutions LLC (collectively "Mesquite et al.") hereby submit their Post-Hearing Brief in support of the May 29, 2008 Settlement Agreement ("Settlement Agreement") which was filed on May 29, 2008 in the above-captioned and above-docketed proceedings. Mesquite et al. are signatory parties to the Settlement Agreement, and they provided testimony in support of the Settlement Agreement during the evidentiary hearings which were conducted thereon on July 9-11, 2008 and July 14-16, 2008.

In this Post-Hearing Brief, Mesquite et al. will discuss certain aspects of the Settlement Agreement which directly affect their respective interests, and which were the subject of the Prepared Testimony of Mesquite et al. witnesses Leesa Nayudu and Greg Bass that was filed in support of the Settlement Agreement in the aforesaid proceedings. That Prepared Testimony was

received into evidence as Mesquite Exhibit No. 1 on July 11, 2007; and, the substance thereof is incorporated herein as background information by this reference.

II.

PROPOSED RATE INCREASE

As indicated in both the Prepared Direct Testimony of Leesa Nayudu, which Mesquite et al. filed on February 29, 2008 [Mesquite Exhibit No. 2], and in the aforementioned Mesquite Exhibit No. 1 joint testimony, Mesquite et al. believe it is important that Tucson Electric Power Company ("TEP") be afforded an opportunity to receive revenues sufficient to enable it to remain a creditworthy purchaser in the competitive wholesale electrical market in Arizona. This is particularly important for a company like TEP, which anticipates that its need to look to that market in satisfaction of its power requirements will continue to steadily increase annually for the foreseeable future. [Tr. 125, l. 6-17]

In that regard, TEP witness David Hutchens testified that in 2007, TEP's fuel mix was "22 percent gas and purchased power and 78 percent coal." [Tr. 815, l. 3-4] But, and of critical importance to its creditworthiness, TEP has begun to experience a "3 percent annual migration from coal to gas and purchased power. So it is a 6 percent swing." [Tr. 817, l. 21-Tr. 818, l. 1] Thus, for 2008, TEP is

"expecting about 25 percent of our demand to be served with gas and purchased power; in 2009, roughly 28 percent; 2010, 31 percent, and so on..." [Tr. 818, l. 4-6]

In addition, in response to a series of questions posed by Commissioner Pierce, TEP witness James Pignatelli testified that of the approximately 3,700 MW of demand TEP currently projects for its electric system by 2025, approximately 30 percent to 40 percent of that demand will be satisfied through purchased power arrangements and natural gas purchases. [Tr. 162, l. 23-Tr. 164, l. 7]

Mesquite et al. are not in a position to independently determine that level of rate increase needed by TEP to achieve and maintain the requisite creditworthiness, and at the same time remain with the constitutional spectrum of "just and reasonable" rates. However, by virtue of its

1 execution of the Settlement Agreement, TEP presumably has concluded that the approximately
2 6% increase over average base rates therein provided for, when examined in the overall context
3 of the Settlement Agreement, will provide it with an opportunity to achieve and maintain that
4 creditworthiness which will enable it to continue to be an active participant in the competitive
5 wholesale electric market in Arizona for the foreseeable future. Similarly, by its execution of the
6 Settlement Agreement, the Commission's Staff has also presumably concluded that the aforesaid
7 6% increase is "just and reasonable," and in the "public interest," when examined in the overall
8 context of the Settlement Agreement. Given these considerations, and absent any information
9 available to them which would suggest that the aforesaid conclusions of TEP and the
10 Commission's Staff are not well-founded, Mesquite et al. support the proposed 6% increase over
11 average base rates provided for in the Settlement Agreement, and recommend Commission
12 approval of the same.

13 III.

14 PURCHASED POWER AND FUEL ADJUSTMENT CLAUSE

15 As TEP witness Pignatelli testified, Commission approval of the Purchased Power and
16 Fuel Adjustment Clause ("PPFAC") provided for in Section VII of the Settlement Agreement
17 would substantially enhance TEP's creditworthiness and viability as a purchaser in the
18 competitive power market. [Tr. 123, l. 10-17] In fact, given TEP's anticipation that purchased
19 power and natural gas-fired generation will steadily increase their respective roles in TEP's
20 generation resource base for the foreseeable future, representing a combined 30 percent to 40
21 percent of its projected total power resources by 2025 [Tr. 163, l. 20-Tr. 164, l. 7], it is
22 reasonable to conclude that TEP's ability to maintain its current creditworthiness might be
23 placed in serious jeopardy, absent a PPFAC such as that provided for in the Settlement
24 Agreement. [Tr. 125, l. 18-21]

25 In this regard, it is important to recognize that the absence of a PPFAC, or the existence
26 of an inadequate PPFAC for a company such as TEP, can result in higher rates for its ratepayers.
27 As TEP witness Pignatelli noted, the absence of a PPFAC or the existence of an inadequate
28 PPFAC can result in undercollections by the utility of the actual purchased power and fuel

1 expenses it is incurring in order to satisfy the requirements of its customers. These
2 undercollections, in turn, can result in two (2) types of problems which adversely affect the
3 utility's ratepayers. First, the utility's providers of purchased power and fuel may require letters
4 of credit or performance bonds from the utility, in order to insure that they will be paid for the
5 power or fuel which is being provided. Either of these credit-enhancing devices will increase the
6 cost of the transaction in question to the utility; and, ultimately that increased cost will be borne
7 by the utility's customers. Second, to the extent there is a significant time lag between when the
8 utility incurs the purchased power and fuel expenses in question, and when it recovers the same
9 from its ratepayers, some ratepayers may be paying a higher unit cost for demand caused by
10 customers who have since left the utility's system. [Tr. 131, l. 11-Tr. 134, l. 8]

11 Accordingly, for the reasons discussed above, Mesquite et al. believe it is imperative that
12 TEP have a well-conceived and well-designed PPFAC as a part of its approved rates and
13 charges; and, subject to the discussion set forth in Section IV below, they further believe that the
14 PPFAC which is provided for in Section VII of the Settlement Agreement is suitable for that
15 purpose, and thus should be approved by the Commission.

16 IV.

17 TEP COMPLIANCE WITH RECOMMENDED BEST PRACTICES 18 FOR PROCUREMENT, AS ADOPTED IN DECISION NO. 70032

19 As noted above, Mesquite et al.'s support for the PPFAC provided for in the Settlement
20 Agreement is expressly conditioned upon TEP's ongoing compliance with the Recommended
21 Best Practices For Procurement ("Best Practices"), which were adopted by the Commission on
22 December 4, 2008 in Decision No. 70032. In that regard, both TEP witnesses Pignatelli and
23 Hutchens testified that TEP is currently in compliance with the Best Practices, and that the
24 company will continue to comply with the Best Practices in the future. [Tr. 134, l. 8-13 and Tr.
25 135, l. 1-17 (Pignatelli); and Tr. 834, l. 5-Tr. 835, l. 18 and Tr. 838, l. 4-Tr. 839, l. 9 (Hutchens),
26 respectively]

27 In addition, Mesquite et al.'s support for the PPFAC provided for in the Settlement
28 Agreement, and for the associated Proposed Plan of Administration ("POA") attached as Exhibit

No. 6 to the Settlement Agreement, is also expressly conditioned upon the Commission's approval and the Commission Staff's utilization of that process and those procedures for implementation and administration of the PPFAC and the POA which Commission Staff witnesses Ernest Johnson and Barbara Keene described in detail during the evidentiary hearings on the Settlement Agreement. [Tr. 364, l. 15-Tr. 372, l. 24 (Johnson); and, Tr. 909, l. 10-Tr. 911, l. 12, and Tr. 912, l. 20-Tr. 914, l. 11 (Keene), respectively] Among other matters, Commission Staff witnesses Johnson and Keene discussed how they envisioned the provisions of Sections 5 through 9 of the POA should be implemented and administered by the Commission and the Commission's Staff; and, Mesquite et al. agree with and support the recommendations of Commission Staff witnesses Johnson and Keene. In that regard, Mesquite et al. believe that the Commission's approval and the Commission Staff's utilization of the aforesaid process and procedures will benefit TEP's ratepayers, signatory parties to the Settlement Agreement and other "interested parties," as referred to in the POA.

V.

**STATUS OF TEP'S CERTIFICATE OF
CONVENIENCE AND NECESSITY**

Mesquite et al. support the approach reflected in Section XII of the Settlement Agreement with regard to the status of TEP's Certificate of Convenience and Necessity ("CC&N") in relation to retail electric competition. At present, TEP's CC&N is open to the prospect of retail electric competition, and TEP's currently authorized tariffs provide for the prospect of direct access customers. In its Application in Docket No. E-01933A-07-0402, TEP proposed that its CC&N be closed to the prospect of retail electric competition in the future, in the event that TEP's post-2008 rates were established on the basis of cost-of-service regulation. TEP subsequently altered its position in that regard, and has agreed to the approach to the "issue of exclusivity" reflected in Section XII.

In essence, that approach preserves the status quo of TEP's CC&N pending such further action on the subject of retail electric competition as the Commission may elect to pursue. In light of the decision reached by the Commission during its August 27, 2008 Open Meeting in

1 Docket No. E-03964A-06-0168, the approach reflected in Section XII of the Settlement
2 Agreement is most appropriate. More specifically, on August 27, 2008 in Docket No. E-
3 03964A-06-0168, the Commission decided to suspend its processing of Sempra Energy Solution
4 LLC's Application for an Electric Service Provider CC&N, authorizing it to provide competitive
5 retail electric service in the certificated service areas of TEP, Arizona Public Service Company
6 and Salt River Project, pending the conduct of workshops and the preparation of a report by the
7 Commission's Staff on the subject of retail electric competition. The approach to the "issue of
8 exclusivity" provided for in Section XII of the Settlement Agreement is fully consistent with this
9 interim development and accordingly should be approved.¹

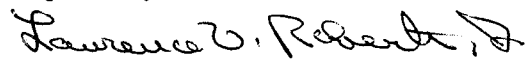
10 VI.

11 CONCLUSION

12 For the reasons discussed above, Mesquite et al. recommend that the Commission enter
13 an Opinion and Order approving the Settlement Agreement and Exhibits 1 through 8 thereto.

14
15 Dated this 28th day of August 2008.

16 Respectfully submitted,

17 

18 Lawrence V. Robertson, Jr.
19 Attorney for Mesquite Power, L.L.C.,
20 Southwestern Power Group II, L.L.C., Bowie
21 Power Station, L.L.C. and Sempra Energy
Solutions LLC

22 The original and fifteen (15) copies of the
23 foregoing Post-Hearing Brief will be filed
24 with the Commission's Docket Control
on August 29, 2008.

25 Copies of the foregoing Post-Hearing Brief
26 will be emailed/mailed on August 29, 2008
27 to the following:

28 ¹ In that regard, the provisions of Section XIII ("Returning Customer Direct Access Charge") of the Settlement Agreement are also fully consistent with this interim development, and should also be approved.

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All Parties of Record

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